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In the Supreme Court of the United States

OCTOBER TERM 1941.

Supreme Court, U. S.
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CHARLES ELMORE CROPLEY
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No. ~~1016~~. 40

GUY T. HELVERING,
Commissioner of Internal Revenue,
Petitioner,

vs.

THE OHIO LEATHER COMPANY,
Respondent.

No. ~~1018~~. 42

GUY T. HELVERING,
Commissioner of Internal Revenue,
Petitioner,

vs.

WARREN TOOL CORPORATION,
Respondent.

JOINT BRIEF IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

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In the Supreme Court of the United States

OCTOBER TERM 1941.

No. 1016.

GUY T. HELVERING,
Commissioner of Internal Revenue,
Petitioner,

vs.

THE OHIO LEATHER COMPANY,
Respondent.

No. 1018.

GUY T. HELVERING,
Commissioner of Internal Revenue,
Petitioner,

vs.

WARREN TOOL CORPORATION,
Respondent.

JOINT BRIEF IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

PRELIMINARY STATEMENT.

This is a joint brief submitted by the respondents in *Helvering, Commissioner v. The Ohio Leather Company,* No. 1016, and *Helvering, Commissioner v. Warren Tool Corporation,* No. 1018, in opposition to the Commissioner's petitions for writs of certiorari to the United States Circuit Court of Appeals for the Sixth Circuit to review its judgments (R. Leather 27; R. Tool 44)[1] entered in the

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[1] Record in *Ohio Leather Co.* case is designated: "(R. Leather ....)"; record in *Warren Tool Co.* case is designated "(R. Tool ....)."

two cases on December 9, 1941. The issues in these two cases are similar enough to warrant the filing of a joint brief[2] at this stage of the proceedings. Other than a common interest in the questions here involved, these two corporations, their officers and shareholders, are complete strangers to each other. The Ohio Leather Company and the Warren Tool Corporation (mistakenly designated sometimes by the Petitioner as Warren Tool Company) reserve the right to present their separate arguments in separate briefs and on oral hearing in event this Court should grant the writs.

OPINIONS BELOW.

Neither of the opinions of the United States Board of Tax Appeals (R. Leather 9-13; R. Tool 24-31) are officially reported. The memorandum opinions of the Sixth Circuit Court of Appeals (R. Leather 27; R. Tool 44) are reported in 124 F. (2d) 397.

JURISDICTION.

The judgments of the Circuit Court of Appeals were entered on December 9, 1941 (R. Leather 27; R. Tool 44). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED IN THE CASES.

The tax involved is imposed by Section 14(b) of the Revenue Act of 1936 on the corporations' "undistributed net income" which is defined in Section 14(a)(2) as "the adjusted net income minus the sum of the dividends paid credit provided in Section 27 and the credit provided in Section 26(c), relating to contracts restricting dividends."

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[2] The Petitioner, for his reason for granting the writ in the *Warren Tool* case merely refers to his argument in the application in the *Ohio Leather* case.

The controversy is over the allowance of credits under Section 26(c)(2) (set out in full in the Appendix) of sinking fund payments required under trust indentures. The Commissioner contends that the taxpayers are not entitled to the credits because the percentages of the net earnings were not payable until the year following the taxable years. The taxpayers contend that they are entitled to the credits because they were required by the terms of their respective indentures to irrevocably set aside within the taxable years such respective amounts, and that upon consideration of their estimated net earnings toward the end of each taxable year they did so irrevocably set aside—by actually paying to their respective trustees the amounts claimed as deductions.

STATUTES AND REGULATIONS INVOLVED.

The statutes and regulations involved are set out in the Appendix *infra*.

STATEMENT.

Each of the taxpayers is an Ohio corporation and each, prior to the critical date, May 1, 1936, issued obligations pursuant to trust indentures. Under the terms of each indenture each taxpayer was required to make sinking fund payments.

Thus, it was provided in Article Two of the Ohio Leather Company indenture that:

> "Section 1. The Company covenants that, to create a Sinking Fund for the further security of the Debentures issued hereunder, it will pay to the Trustee • • • on or before the next succeeding first day of April, • • • an amount equal to ten per cent (10%) of the net earnings earned by the Company during the fiscal year ending on the thirty-first day of the next preceding December, as such net earnings are defined hereinafter in this Article, which sums and amounts shall be held by the Trustee for the security of all

outstanding Debentures until paid out as hereinafter provided. * * *

"Section 2. On or before April 1, 1937, and thereafter annually on or before April 1st in each year to and including April 1, 1945, the Company will cause Ernst & Ernst of Cleveland, Ohio, or such other certified public accountant or accountants as may be approved by the Trustee hereunder, to determine the amount, if any, of the net earnings of the Company for the fiscal year ended the last preceding December 31st.

* * * * * *

"Section 5. * * *

"In lieu of payment of cash into the Sinking Fund as above provided in Section 1 of this Article, the Company may deliver to the Trustee, to apply upon such payments, Debentures issued hereunder with all unmatured coupons attached thereto, which have previously thereto been issued, sold and repurchased by the Company or otherwise acquired by the Company, and in each such event shall have credit therefor to the extent of the principal amount of such Debentures (but without accrued interest or premium thereupon) so delivered to the Trustee. The fact of re-purchase or re-acquisition by the Company shall be disclosed to the Trustee by a certificate with respect thereto delivered by the Company to the Trustee at the time of the delivery of said Debentures. The Company may, but need not, anticipate payments to the Sinking Fund either in cash or in Debentures and have credit therefor on its thereafter accruing obligation or obligations to pay moneys or deposit Debentures for the Sinking Fund." (R. Leather 10-11.)

And in the Warren Tool indenture in Article Four it was similarly provided that:

"Section 1. For the purpose of creating the sinking fund for the redemption of the bonds issued hereunder, the Company hereby agrees to pay to the Trustee on or before the 1st day of April, 1935, and on or before the 1st day of April of each year thereafter to and including April 1, 1942, a sum of money equal to Twenty-five Per Cent (25%) of its net earnings for

the calendar year next preceding. * * * The Company may, in lieu of depositing cash in whole or in part, purchase bonds issued hereunder at a price not exceeding the redemption price thereof as fixed by the provisions of Article V hereof, and deliver such bonds to the Trustee for credit against said sinking fund obligations to the extent of the purchase price (excluding the accrued interest) paid therefor by the Company. * * * Prior to the first day of April in each year abovementioned, the Company shall also file with such Trustee a statement sworn to by one of such officers showing the amount of the Company's net earnings for the preceding calendar year computed in the manner hereinbefore provided and duly certified by such accountant or accountants." (R. Tool 25; as corrected for typographical error by typewritten stipulation filed in C. C. A. 6, March 7, 1941.)

The credits claimed are credits for payments made (by the deposit of bonds) within the taxable years towards the end of each year after computations of the respective taxpayer's apparent profits had been made. Both the taxable years 1936 and 1937 are involved in the Warren Tool case. Only the taxable year 1936 is involved in the Ohio Leather case. The actual credits claimed and allowed by both the Board of Tax Appeals and the Circuit Court of Appeals are the percentages of the net earnings as finally determined. Thus, for example, in the Ohio Leather Company case the taxpayer, on December 14, 1936, estimated that its net earnings for that taxable year would be about $220,000.00 (R. Leather 24) and accordingly deposited $22,000.00 in bonds on this obligation. As a matter of fact, the actual earnings turned out to be $209,493.62 (R. Leather 25), and accordingly the actual credit claimed is only $20,949.36, being 10% of the net earnings for the taxable year. Similarly, Warren Tool Corporation made, in December of 1936 and also in December of 1937, such payments in amounts determined in like manner.

ARGUMENT.

REASONS FOR DENYING THE WRITS.

A. There is no real conflict between the decision in the Strong Mfg. Co. case, the decision below and the decidecision of the Fourth Circuit in the Antietam Hotel case. The difference is one of facts.

There is here involved no question of importance[1] in Federal tax law. The statute is no longer in force. The Sixth Circuit Court of Appeals, in applying the statute, followed settled rules of construction. The Commissioner does not contend otherwise, but does suggest that a conflict exists between the decisions of the Sixth Circuit in these cases (and also its decision in *Commissioner v. Strong Mfg. Co.*; 124 F. (2d) 360, certiorari applied for; No. 1017, this being the case on which the Circuit Court based its decisions in the *Ohio Leather* and *Warren Tool* cases) and the decision of the Fourth Circuit Court of Appeals in *Antietam Hotel Corp. v. Commissioner*, 123 F. (2d) 274. We think this suggestion of conflict is error. The petitioner's statement in its Reason For Granting the Writ that:

> "* * * the court below relied upon its opinion in a companion case, *Commissioner v. Strong Manufacturing Co.*, 124 F. (2d) 360, in which it recognized that its decision was contrary to *Antietam Hotel Corp. v. Commissioner*, 123 F. (2d) 274 (C. C. A. 4th). The decision herein is likewise in conflict with the *Antietam* case, in which a corporation was required for sinking

[1] In his brief oppo ng the granting of the Writ of Certiorari in *Moloney Electric Co. v. Commissioner*, Nos. 659-660, certiorari denied November 10, 1941, rehearing denied January 12, 1942, the Commissioner said:

> "Contrary to petitioner's assertion (Pet. 6), the cases do not present any important issue of Federal law which this Court should determine. They merely involve claims to credits in the computation of the surtax imposed by the Revenue Act of 1936 upon undistributed corporate profits, and their outcome turns not on any new or far-reaching principle of law, but on the particular facts."

> fund purposes to pay to trustees on March 20 of each year 60 percent of its net earnings for the preceding calendar year. The Fourth Circuit denied the credit under Section 26 (c) (2) since the contract did not require the earnings to be irrevocably set aside within the taxable year. Cf. *Helvering v. Moloney Electric Co.*, 120 F. (2d) 617 (C. C. A. 8th), certiorari denied, November 10, 1941, Nos. 659-660, present Term, rehearing denied, January 12, 1942." (Commissioner's Pet. Ohio Leather, pp. 4, 5.)

refers to the following from the opinion of the Sixth Circuit Court of Appeals in the *Strong* case:

> "We are mindful of the fact that since the argument in the instant case, in *Antietam Hotel Corp. v. Commissioner of Internal Revenue*, 4 Cir., 123 F. 2d 274, it was held 'that as an indispensable condition precedent to the allowance of the credit, the contract itself must in terms require that a portion of the earnings and profits of the taxable year be * * * irrevocably set aside within the taxable year.' We do not arrive at the same conclusion, for we do not find from the language of the statute that the contract must require the earnings to be irrevocably set aside, in terms. With regard to the case of *Helvering v. Moloney Electric Co.*, 8 Cir., 120 F. 2d 617, in which it was held that the taxpayer was not entitled to credit under the section of the statute in question, it appears that there was no showing in that case what the earnings of the corporation were, when the payment on the indebtedness was made, or whether the payment was ever made because of any contract requirement; and these circumstances were of paramount significance in that adjudication. Confronted by entirely different facts, it would appear that further discussion, for the purpose of distinguishing the cited case, would be fruitless." (124 F. 2d 360, 365-6.)

The *Antietam* decision of course contained the language quoted in the above excerpt from the Court's opinion in the *Strong* case, indicating that the Fourth Circuit, *if it had had to pass* on that question, would have for that

reason denied the credit. That the taxpayer in the *Antietam* case was in fact in no position to obtain the credit under the principles of the *Strong* case is shown by difference in the facts, a situation recognized by the Board of Tax Appeals* for, in denying the credit in the *Antietam* case, it first pointed out that the funds were never segregated during the taxable years but remained in the general bank account. *The credit by the statute is limited "to the extent that such amount has been so paid or set aside."* The Board in the *Antietam* case said:

> "We have considered the general question involved in the instant proceeding in two recent opinions. In *Strong Mfg. Co.*, 41 B. T. A. 1273 (Dec. 11,122), wherein the taxpayer was granted a credit, it appears that the company anticipated its income for the taxable year and actually did make the payments within the taxable year there in question. *Therein the facts differ materially from our instant case.*
>
> In June of 1940 this Board decided the case of *Moloney Electric Co.*, 42 B. T. A. 78 (Dec. 11,214), which considered a similar question. In this later case we found against the taxpayer. We said that in the *Strong* case the creditors had an equitable lien throughout the entire taxable year recognized by the taxpayer, whereas in the *Moloney* case the creditor had no equitable lien upon the taxpayer's earnings unless and until they should be in excess of $320,000. While there was a payment of certain moneys within the taxable year by the taxpayer in the *Moloney* case, we said:
>
> > The record does not disclose whether the payment was made near the close of the year when it was apparent that the earnings would be in excess of $320,000, or whether it was made earlier in the year when the earnings were much less than that amount.
>
> In our instant case [i.e., the *Antietam* case], although the petitioner insists that the bondholders had

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*In its memorandum opinion entered October 23, 1940 and reported *C. C. H. Board of Tax Appeals Service*, Dec. 11,357-A.

an equitable lien, the contract expressly provides that they were entitled to nothing provided the net profits, calculated according to the indenture, did not exceed $10,000. Consequently, we have a situation analogous to that of the *Moloney* case with the exception that in our present case nothing was physically transferred within the taxable year. Our lien, if such it be, is closely comparable to the lien of that case. There the Board, although recognizing that a lien may have existed at some time, nevertheless, denied the taxpayer a credit. We must here follow the holding of the *Moloney* case. * * * Furthermore, a stronger factor is here present which was not discussed in the *Moloney* case. There was no actual payment here within the taxable year, nor any visible setting aside of funds. Therefore, it can not be said that all of the requirements of the statute have been fulfilled.

For the above reasons we must hold in favor of the respondent.

Decision will be entered under Rule 50." *C. C. H. Board of Tax Appeals Service*, Dec. 11,357-A, p. 33,150.

Further evidence that there was no "issue" (as Petitioner claims, Pet. Ohio Leather, 5) in the *Antietam* case as to whether or not a contract *must in express terms* require the earnings be set aside with the taxable year, is found in the opinion of the Fourth Circuit in quoting the facts found by the Board of Tax Appeals:

"The corporation [Antietam Hotel] made no entry on its books between January and March of 1937 or 1938 relative to the sinking fund payments. The balance sheet of the petitioner for the year ended December 31, 1936 carried a notation thereon as follows:

'Sinking Fund payment due March 20, 1937, $4,642.09.' and for the year ended December 31, 1937:

'Sinking Fund payment due March 20, 1938, $13,527.32.'

The percentage of net earnings of petitioner as defined in Section 3 of the Supplemental Indenture, *supra, was held in the general bank account* of the cor-

poration until March of the years following. (123 F. 2d 274, 275-6.)

• • •

Since the organization of the petitioner, James Mullen of Richmond, Virginia, has been associated with it either as assistant secretary or acting as secretary and its counsel; and during the years 1936 and 1937 he attended the Board meetings and advised the executive committee. He *advised them* that the money must be set aside as of December 31st of each year and must be held separate and not used for any purpose other than the payment to the trustee. He *advised them* that it constituted a trust fund which they could not use and that they themselves would become personally liable if they permitted it to be used." (Emphasis ours.) (123 F. 2d 274, 276.)

Then in its opinion the court said:

"Petitioner contends very strenuously that the applicable law of Maryland treats this indenture as an express trust, and that, accordingly, the funds covered by the indenture cannot be diverted from the ultimate use set out in the indenture without the violation of a duty under the trust. Consequently, petitioner claims that there was in this case an irrevocable setting aside of the funds by operation of law. *It is clear from the record, however, that these funds were never actually segregated* from the taxpayer's other moneys during the taxable years in question. Indeed, the evidence discloses that during the taxable years in question, *the funds actually remained in petitioner's general bank account, and it is quite clear that actual payments to the Trustee were not made during the taxable years* but were, in each instance, paid by check during March of the year after the taxable year. Thus, *there was no definitive act within the taxable year which divested the corporation's control over the funds.*". (Emphasis ours.) (123 F. 2d 274, 276.)

After the Court quoted Regulations 94, Art. 26(c)(2) set out in full in the appendix, the Court said:

"Thus, it will be noted that the Treasury Regulation restricts the credit to amounts *actually* set aside

within the taxable year. Although such an interpretation is not binding on this Court, it is highly persuasive at least." (Emphasis the Court's.) (123 F. 2d 274, 277.)

In view of the foregoing, we respectfully insist that there is no conflict between the *Strong* case and the *Antietam* case for the issue decided in the *Strong* case was never present in the *Antietam* case, since in the *Antietam* case there had been no actual setting aside within the taxable year as required by the statute and it therefore was no concern of the Fourth Circuit whether or not the statute makes it mandatory that the contract require *in terms* the setting aside within the taxable year.

The expression of the Court in the *Strong* case that it did not reach the "same conclusion" as the Fourth Circuit in the *Antietam* case was accordingly dictum since the Fourth Circuit under the facts had no need in its disposition of the case to reach "a conclusion" on this point. Likewise, the member of the Board of Tax Appeals in *A. E. Staley Manufacturing Company v. Commissioner*, 46 B. T. A. .... (No. 26) January 27, 1942, when he said that the opinions of the two circuits are "apparently in conflict * * * on the question as to whether, under Section 26(c)(2), the contractual provision must *in terms* require that a portion of the earnings and profits of the taxable year be irrevocably set aside or paid within the taxable year," was guilty of either dictum or insufficient analysis of the two cases. In the *Staley* case the taxpayer had made its "anticipatory payment" by delivering in cash, in December of the taxable year, an amount equal to the required percentage of the estimated net earnings. The contract (trust indenture) in this case specifically forbade such a procedure by its exact terms, for it provided:

> "* * * no anticipated sinking fund payment may be made in cash:" (p. 2 of the advance sheet of the *Staley* decision.)

On the basis of this provision, the Board of Tax Appeals in the *Staley* case held that even under the decision in the *Strong* case the credit should be denied to the taxpayer in the *Staley* case, and in so doing, in effect, reached the same conclusion that Respondents herein contend is controlling, *viz*: that each case turns on its own facts.

B. The judgments below were correct.

The Commissioner has refrained from filing a brief in support of his petition—relying on the asserted conflict. We believe we have shown above that this "conflict" is not within the following principle which this Court has told the bar it strives to maintain, *viz.*:

> "* * * that it is very important that we be consistent in not granting the writ of certiorari except in cases involving principles the settlement of which is of importance to the public as distinguished from that of the parties, and in cases where there is a real and embarrassing conflict of opinion and authority between the circuit courts of appeal." Taft, *C.J.* (*Layne & Bowler Corporation v. Western Well Works, Inc., et al.*, 261 U. S. 385, at p. 393.)

These cases are not of public importance. The tax was so drastically changed by Sections 13 and 27(a)(4) of the Revenue Act of 1938 (since it was so unsatisfactory in operation) that a decision in these cases would afford little or no aid in any cases under subsequent acts. (*Mertens Law of Federal Income Taxation, 1939 Supplement*, § 32B.02, page 1499.

Since the Commissioner has not indicated in what respect, if any, the decision of the Sixth Circuit Court of Appeals in *Commissioner v. Strong Manufacturing Company*, 124 F. (2d) 360, on which that court based its judgments in the *Ohio Leather* and the *Warren Tool* cases, was in error, the taxpayers here will refrain from a lengthy discussion of the opinion below. After stating the facts as found by the Board of Tax Appeals, the court in the *Strong*

case said that the critical question was whether or not the construction claimed for the statute by the Commissioner, namely, that "to set aside" required a physical separation or appropriation, was correct. It pointed out that such a construction would forbid credits to any corporation whose business was such that it could not definitely ascertain its profits on the last day of the year and thus deny the credit to all manufacturing and merchandising companies and grant it only to financial institutions.* It relied on the fundamental principle of statutory construction that the intention of the legislature is the most important guide and to ascertain that intention it will be presumed that unfair, undue hardship was not intended. Further guides for ascertaining the intention of the legislature used by the court were the principles that substance and not form controls in taxing statutes and that the title and the legislative scheme or plan, which was the object of the act, may be examined. The court termed, rightly we believe, the contention of the Commissioner as one that would result in an "unreasonable, capricious, and discriminatory plan of taxation," 124 F. (2d) 360, 365, which should be held to be contrary to the Congressional intention.

Finally in applying the statute with the foregoing principles, both the Board of Tax Appeals and the Sixth Circuit Court of Appeals held that under the facts (i.e. both the terms of the trust indentures and the specific payments) each of the taxpayers met the requirements for credits under Section 26(c)(2) of the Revenue Act of 1936. We believe that additional authorities or arguments of our own to further demonstrate the correctness of the court's judgments would be here inappropriate since the Commissioner has not filed a brief; however, we do desire to note that the Commissioner in the entire course of the con-

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* Financial institutions were exempt from this tax. Section 107 of the Revenue Act of 1936; c. 690, Title I, Section 104, 49 Stat. 1677.

troversies has never shown how Section 26(c)(2) should be construed to give relief to any corporation which was required to pay or set aside a percentage or portion* of its year's earnings and profits to a sinking fund. Any such construction would, we submit, inevitably include these taxpayers.

CONCLUSION.

For the reasons shown above, we respectfully submit that there is not a conflict of opinion and authority between the Circuit Courts of Appeals or error in the result reached by the Sixth Circuit Court of Appeals in its judgments in these cases or a question of great public importance and accordingly the petitions for the writs of certiorari should be denied.

Respectfully submitted,

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* As shown *supra*, Congress included in Section 26(c)(2) the provision: "* * * a requirement to pay or set aside an amount equal to a percentage of earnings and profits shall be considered a requirement to pay or set aside such percentage of earnings and profits. * * *" This provision and the phrase "irrevocably set aside within the taxable year for the discharge of a debt" also in the statute, unmistakably manifest the intention of Congress to meet situations where the payment was postponed so that the payment or setting aside would include a portion or percentage of the profits of an entire year. As already stated by this Court this surtax on undistributed profits is one "* * * imposed on profits earned during a definite period—a tax year—* * *" *Helvering v. Northwest Steel Mills*, 311 U. S. 46, 53 (1940). It is equally manifest, we believe, that should a corporation after the accumulation of earnings and profits dissipate these earnings and profits before the final date for an accounting under the trust indenture, it, the corporation, would breach its contract and the trustee, if it knowingly acquiesced in such conduct, would be guilty of [illegible]

APPENDIX.

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 14. SURTAX ON UNDISTRIBUTED PROFITS.

(a) *Definitions.*—As used in this title—(1) The term "adjusted net income" means the net income minus the sum of—

(A) The normal tax imposed by section 13.

* * * * *

(2) The term "undistributed net income" means the adjusted net income minus the sum of the dividends paid credit provided in section 27 and the credit provided in section 26 (c), relating to contracts restricting dividends.

(b) *Imposition of Tax.*—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation a surtax equal to the sum of the following, subject to the application of the specific credit as provided in subsection (c):

7 per centum of the portion of the undistributed net income which is not in excess of 10 per centum of the adjusted net income.

12 per centum of the portion of the undistributed net income which is in excess of 10 per centum and not in excess of 20 per centum of the adjusted net income.

* * * * *

SEC. 26. CREDITS OF CORPORATIONS.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

* * * * *

(c) *Contracts Restricting Payment of Dividends.*—

* * * * *

(2) *Disposition of Profits of Taxable Year.*—An amount equal to the portion of the earnings and profits of the taxable year which is required (by a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with

the disposition of earnings and profits of the taxable year) to be paid within the taxable year in discharge of a debt, or to be irrevocably set aside within the taxable year for the discharge of a debt; to the extent that such amount has been so paid or set aside. For the purposes of this paragraph, a requirement to pay or set aside an amount equal to a percentage of earnings and profits shall be considered a requirement to pay or set aside such percentage of earnings and profits. As used in this paragraph, the word "debt" does not include a debt incurred after April 30, 1936.

* * * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 26-2. *Credit in connection with contracts restricting payment of dividends.*—(a) The credit provided in section 26 (c) with respect to contracts restricting the payment of dividends is not available under every contract which might operate to restrict the payment of dividends, but only with respect to those provisions of written contracts executed by the corporation prior to May 1, 1936, which satisfy the conditions prescribed in the Act. The charter of a corporation does not constitute a written contract executed by the corporation within the meaning of section 26 (c). The provisions recognized by the Act are of two general types, as follows:

(1) Those which come within section 26 (c) (1), in that they prohibit or limit the payment of dividends during the taxable year; and

(2) Those which come within section 26 (c) (2), in that they require the payment, or irrevocable setting aside, within the taxable year, of a specified portion of the earnings or profits of the taxable year for the discharge of a debt incurred on or before April 30, 1936.

* * * * * *

(c) *Disposition of profits of ~~taxable~~ year.*—Under the provisions of section 26 (c) (2), a corporation is allowed a credit in an amount equal to that portion

of the earnings and profits of the taxable year which, by the terms of a written contract executed by the corporation prior to May 1, 1936, and expressly dealing with the disposition of the earnings and profits of the taxable year, it is required within the taxable year to pay in, or irrevocably to set aside for, the discharge of a debt incurred on or before April 30, 1936. The credit is limited to that amount which is actually so paid or irrevocably set aside during the taxable year pursuant to the requirements of such a contract.

Only a contractual provision which expressly deals with the disposition of the earnings and profits of the taxable year shall be recognized as a basis for the credit provided in section 26 (c) (2). A corporation having outstanding bonds is not entitled to a credit under a provision merely requiring it, for example, (1) to retire annually a certain percentage or amount of such bonds, (2) to maintain a sinking fund sufficient to retire all or a certain percentage of such bonds by maturity, (3) to pay into a sinking fund for the retirement of such bonds a specified amount per thousand feet of timber cut or per ton of coal mined, or (4) to pay into a sinking fund for the retirement of such bonds an amount equal to a certain percentage of gross sales or gross income. Such provisions do not expressly deal with the disposition of earnings and profits of the taxable year. A contractual provision, however, shall not be considered as not expressly dealing with the disposition of earnings and profits of the taxable year merely because it deals with such earnings and profits in terms of "net income," "net earnings," or "net profits."

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